> the machine in and lose it for 7-10 days – plus the time going through this crap. So I have this new machine and paid for them to FUCKING FIX IT IN MY HOUSE and they don't and I lose it for two weeks. DELL SUCKS. DELL LIES. Put that in your Google and smoke it, Dell.

The 6/21/05, anti-Dell Blog on BuzzMachine attracted worldwide attention – and support.

136. On 6/28/05, AMD issued a release describing a suit it had filed against Intel, alleging antitrust violations, including ***secret illegal rebates/kickbacks to Dell***:

> **AMD Files Antitrust Complaint Against Intel In U.S. Federal District Court**
>
> * * *
>
> This litigation follows a recent ruling from the Fair Trade Commission of Japan (JFTC), which found that Intel abused its monopoly power to exclude fair and open competition, violating Section 3 of Japan's Antimonopoly Act. These findings reveal that Intel deliberately engaged in ***illegal business practices*** to stop AMDs increasing market share by imposing limitations on Japanese PC manufacturers. ***Intel did not contest these charges.***
>
> ***The European Commission has*** stated ***that it is pursuing an investigation against Intel for similar possible antitrust violations and is cooperating with the Japanese authorities.***

Among the violations alleged in AMD's suit were that Intel:

- ***Forc[ed] major customers such as Dell*** . . . into Intel-exclusive deals in return for ***outright cash payments***, discriminatory pricing or marketing subsidies ***conditioned on the exclusion of AMD*** . . . . [A]s confirmed by the JFTC in Japan, Intel has paid Dell . . . huge sums not to do business with AMD.

137. AMD's actual complaint against Intel alleged:

> **Exclusionary Rebates**
>
> Intel has also imposed on OEMs a system of first-dollar rebates that have the practical and intended effect of creating exclusive or near-exclusive dealing arrangements and artificially foreclosing AMD from competing for a meaningful share of the market. In general, the rebate schemes operate as follows: ***quarterly, Intel unilaterally establishes for each of its customers a target level of purchases of Intel microprocessors. If the customer achieves the target, it is entitled to a rebate on all of the quarter's purchases of <u>all</u> microprocessors – back to the very first one – generally in the neighborhood of 8-10% of the price paid. Intel provides the rebate in cash at the quarter's close. OEMs operate on razor-thin margins, so qualifying for an Intel rebate frequently means the***

difference between reporting a profit or a loss in the coming – and closely watched – quarterly earnings.

138. On 8/11/05, after the close of trading, Dell shocked the markets with ***much lower-than-expected*** 2ndQ F06 results, ***including revenues***. Dell also revealed that its 3rdQ F06 revenue growth would also fall short of its prior forecasts. On 8/12/05, *Investor's Business Daily* reported:

Dell Takes Hit After Its Sales Lag Estimates; Forecast Also Disappointing

Investors dumped shares of Dell Thursday after the computer maker reported quarterly sales below what analysts had expected. It also guided sales forecasts down for the current quarter.

* * *

The sales shortfall came as a shock to Wall Street . . .

"It was definitely a surprise to the Street," said Shaw Wu, an analyst with American Technology Research.

139. On 8/12/05, *Bloomberg* reported:

Shares of Dell Inc. fell 7.4 percent, ***the most in four years***, on signs the revenue surge that transformed the company into the world's largest maker of personal computers is subsiding.

Analysts responded to Dell's report that sales growth fell to the lowest in three years by slicing their recommendations and estimates. Goldman, Sachs & Co.'s Laura Conigliaro, whose firm took Dell public in 1988, ***reduced*** her rating on the stock. Merrill Lynch & Co.'s Steve Milunovich, ranked the No. 2 computer analyst by Institutional Investor magazine, ***reduced*** his estimates.

140. Dell's stock plunged from $40.03 on 8/11/05 to $36.10 on 8/12/05 on huge volume of 96.2 million shares, as the 8/11/05 revelations were inconsistent with and undercut prior Class Period representations. This approximate $10 billion loss of market capitalization in Dell's stock took some of the artificial inflation out of Dell's stock, damaging prior Class Period purchases.

141. While Dell's stock fell sharply after the negative results of 8/11/05, it continued to trade at artificially inflated levels, as defendants failed to make full or complete disclosure and

continued to make false and misleading statements concerning Dell's business, its business model and its finances and financial condition and results, assuring investors that the problems contributing to the financial shortfall had been identified and fixed. For instance, on 8/11/05, Dell held a conference call for analysts, money managers and institutional investors. During this call the following occurred:

> [**Schneider – CFO:**] Dell continued to outperform the market in our second quarter. ***We posted record earnings*** . . . . [W]e generated $13.4 billion in revenue . . . . ***This was below the guidance we gave at the beginning of the quarter***. . . . While we're short on revenue we focused on delivering our earnings commitment. Our operating profit grew 17% year-over-year to $1.2 billion, ***delivering operating margin of 8.7%, an improvement of 10 basis points year-over-year***. . . . We generated pro forma EPS of $0.38, up 23% and in line with our guidance.
>
> * * *
>
> [**Runkle – *Morgan Stanley – Analyst:***] . . . [J]ust in terms of your commentary about misexecuting, as you go back and look at how or why you misexecuted, how are you thinking about that issue . . . .
>
> [**Rollins – *Dell, Inc. – CEO:***] . . . First off, ***our earnings came in exactly as expected***, and the growth rate in terms of units exceeded expectation. The shortfall was in the revenue, ***and I think the issue for us is that . . . we just misexecuted and didn't get the up sell within the consumer business that we normally got and let it get away from us. That's the misexecution that we think we can fix. We know how to do it, we've been doing it now for ten years. We stumbled there, but we'll get it back in line.***
>
> * * *
>
> ***[W]e're not changing our strategy. . . . [W]e'll continue to drive balanced, profitable growth in Q3 and beyond***. . . . [W]e believe there's multiple engines of growth for our company . . . . ***We're confident in our ability to deliver on those commitments*** . . . .

142. On 8/17/05, Prudential issued a report on Dell based on a lunch with Schneider, Dell's CFO, reporting what he told Prudential:

- Yesterday afternoon, we hosted a lunch with Jim Schneider, Dell's CFO.
- ***We left the meeting confident that management has identified and addressed the problem areas which drove the FQ2 revenue shortfall*** . . . .

143. An 8/17/05, Jeff Jarvis "Blogged" an open letter to Dell on "BuzzMachine." The letter stated:

> To: Michael Dell . . . .
>
> CC: Michael George, chief marketing officer and vice president for the U.S. consumer business, Dell
>
> Gentlemen:
>
> Your customer satisfaction is plummeting, your marketshare is shrinking, and your stock price is deflating.
>
> Let me give you some indication of why, from one consumer's perspective. I won't bore you with all the details of my saga of Dell hell; you can read all about it here and here. The bottom line is that a low-price coupon may have gotten me to buy a Dell, ***but your product was a lemon and your customer service was appalling***.
>
> . . . I'm typing this on an Apple Powerbook. I also have bought two more Apples for our home.
>
> But you didn't just lose three PC sales and me as a customer.
>
> ***Today, when you lose a customer, you don't lose just that customer, you risk losing that customer's friends. And thanks to the internet and blogs and consumer rate-and-review services, your customers have lots and lots of friends all around the world.***
>
> I blog. And I shared the story of my Dell travails here. The topic resonated with hundreds more people. Go read the many comments here and here. Too busy? Then have an intern or an MBA do it for you.
>
> And then have them read all the many posts of other bloggers who pointed to my posts and shared their dissatisfaction with your products, service, and brand and, in many cases, announced that they were no longer going to buy your name: See some of those posts here or here and you'll learn a lot.
>
> Heard of those new podcast things? Well, you're in one.
>
> ***Now go read the press this generated, because the press is reading blogs, even if you're not: here (where Fast company turned customer dissatisfaction into a verb: you got Dell'd), here (ZDnet not just in America but in India, where your many customer-service people are probably reading this, even if you're not), here (a mainstream newspaper), here (an influential online news service), here (a consumer PC magazine), here (BusinessWeek, guys), and plenty more here***: Just Google it; you should be doing that every day.

* * *

So allow me to give you some friendly and free advice about these blog things. You can pay for more.

Read blogs. Go to Technorati, Icerocket, Google, Bloglines, Pubsub, and search for Dell and read what they're saying about you. Get it out of your head that these are "bloggers," just strange beasts blathering. ***These are consumers, your marketplace, your customers*** – if you're lucky. They are just people. You surely spend a fortune on consumer research, on surveys and focus groups and thinktanks to find out what people are thinking. On blogs, they will tell you for free. All you have to do is read them. All you have to do is listen.

* * *

Listen to all your bad press and bad blog PR and consumer dissatisfaction and falling stock price and to the failure of your low-price strategy and use that blog to admit that you have a problem. Then show us how you are going to improve quality and let us help. Make better computers and hire customer service people who serve customers.

* * *

Sincerely,

Jeff Jarvis

144. On 8/17/05, *The Philadelphia Inquirer* published an article regarding Dell's declining customer satisfaction:

Dell rated lowest in recent index of client satisfaction; PC buyers cited long waits, unanswered questions. . . .

Dell Inc.'s customer satisfaction fell this year to the lowest rating since 1998 as consumers complained of long wait times for help and trouble getting questions answered.

Customer satisfaction at Dell . . . declined 6.3 percent, as gauged by the University of Michigan's American Customer Satisfaction Index.

Dell's decline may be a sign the company is poised to lose sales, said Claes Fornell, marketing professor and head of the university's National Quality Research Center. . . .

"***Dell is dropping in large part because of call-center problems, including long wait times and difficulty with consumers' getting their questions answered," Fornell said in an interview. "Consumers are also questioning the reliability of their PCs.***"

* * *

> "*The satisfaction of customers is pretty much a leading indicator as to whether customers will come back and buy more*," Fornell said. . . .
>
> ***Dell chairman Michael Dell told analysts last week that internal surveys showed customer satisfaction "improved" in the last quarter, even as PC shipments rose and the number of consumers being served increased.***

145. According to the *Austin American-Statesman*, Rollins refuted the findings. "CEO Kevin Rollins disputed the analysis last week, telling reporters and later analysts that, rather than slipping, ***the company's performance was improving***. A recent ranking from Technology Business Research put Dell No. 1 in customer service for business customers. And the company's own scores for its consumer service have risen 'over the last quarter or so,' Rollins said. 'Our unit volumes are large,' he said. 'So you could actually get more calls, but the percent of calls is going down.'"

146. On 8/25/05, *BusinessWeek Online* published an article that was negative concerning Dell's customer satisfaction, noting the widespread attention given the 8/17/05 BuzzMachine blog activities:

> **Dell: In the Bloghouse; A PC-owner's Web diary of complaints about customer service has yielded heavy traffic and some near-contrition from the maker**
>
> ***PC industry circles have been buzzing in recent months that Dell's (DELL) customer support is slipping – a claim bolstered on Aug. 16 by a University of Michigan study that showed a hefty decline in customer satisfaction from a year ago.*** So the last thing Dell needed was for someone to turn the customer-service issue into a cause celebre.
>
> ***Enter Jeff Jarvis.***
>
> Over the summer, Jarvis began writing in his personal blog, ***BuzzMachine***, about his lengthy quest to fix a $1,600 computer, an ordeal he said included countless e-mails, some unanswered, and phone calls to Dell's customer-service line.
>
> "A LEMON." Jarvis wrote in his blog that he bought a service package including in-home repairs, but when the PC overheated and malfunctioned, he was told to send it in.

It still wasn't working when it came back, however, according to Jarvis. So he launched a series of attacks on Dell, including an Aug. 17 open letter to CEO Michael Dell saying: "***The bottom line is that a low-price coupon may have gotten me to buy a Dell, but your product was a lemon, and your customer service was appalling***."

* * *

John Hamlin, Dell's senior-vice president for the U.S. consumer business, says Dell is ***adding more call centers***, each employing about 2,000 workers, and ***improving training for phone reps***.

"***The customer experience is one of the most important issues for us***," says Hamlin, adding that a year ago, to make sure customers' machines are working, Dell began contacting those who its records show have sought help at least three times over the course of one week.

147. On 8/25/05, *BusinessWeek Online* published a second article – this one about Dell's slowing growth:

What's With the Dell Doldrums?

* * *

[W]hy are Dell shares down 16% since the end of last year . . . .

* * *

[T]he sales number was below its own earlier forecast of a 16% to 18% increase. Worse yet, Dell also ratcheted down its revenue projections for the current quarter ending in October. Dell's stock immediately tanked 7.4%.

INVESTORS' "WHIPSAW." Some analysts are questioning whether Dell stock still deserves its longstanding rating. On Aug. 12, high profile Goldman Sachs analyst Laura Conigliaro downgraded Dell to "market perform" from "Outperform" because of the lower estimate for future sales growth.

148. This negative publicity concerning Dell was furthered when, on 8/30/05, *Moneybox* published an article regarding Dell, headlined and stating:

Is Dell Dying?

* * *

[A]ll of a sudden, Dell is getting walloped. There has been a disappointing earnings report, complaints about customer service, unflattering stock charts, and a rash of articles questioning Dell's future – *Business Week* had two

negative Dell articles in its current issue, and the *Financial Times* had a critical takeout last week.

Dell's disappointing quarter was the proximate cause of the negative press. . . . [I]t represented the first time in several years that Dell failed to meet the earnings estimates. What's more, executives ratcheted down expectations for revenue growth in the current quarter. ***The stock has fallen 11 percent since the announcement.***

* * *

Dell had the bad luck to tick off a very powerful blogger. . . . It was Dell's misfortune that one of those errors affected a person with a huge megaphone, ***blogger Jeff Jarvis***. Jarvis' ***blow-by-blow account of his Dell hell has become an Internet phenomenon.***

149. Dell's stock fell during the second half of 8/05, as this negative information, which undermined and contradicted Dell's earlier and ongoing representations, reached and was digested by the market. Dell's stock fell from $37.05 on 8/18/05 to $35.05 on 8/29/05, a $5 billion loss of market capitalization, damaging prior Class Period purchasers.

150. On 9/1/05, Dell filed its 2ndQ F06 report on Form 10-Q with the SEC, signed by Hooper. The 2ndQ F06 10-Q contained Dell's earlier reported financial results. It also stated:

Second Quarter Performance Highlights

* * *

Operating Income Operating income increased 17% to $1.2 billion for the quarter, or 8.7% of revenue, up from $1.0 billion and 8.6% of revenue in the second quarter of fiscal 2005.

Earnings Earnings per share increased 32% to $0.41 for the quarter.

* * *

Results of Operations

The following table summarizes the results of our operations for the three and six month periods ended July 29, 2005 and July 30, 2004:

	Three Months Ended				Six Month Ended			
	July 29, 2005		July 30, 2004		July 29, 2005		July 30, 2004	
	Dollars	% of Revenue	Dollars	% of Revenue	Dollars	% of Revenue	Dollars	% of Revenue
	(in millions, except per share amounts and percentages)							
Revenue	$13,428	100.0%	$11,706	100.0 %	$26,814	100.0%	$23,246	100.0%
Gross margin	2,499	18.6%	2,134	18.2%	4,990	18.6%	4,207	18.1%
Operating expenses	1,326	9.9%	1,128	9.6%	2,643	9.9%	2,235	9.6%
Operating income	1,173	8.7%	1,006	8.6%	2,347	8.8%	1,972	8.5%
Net income	1,020	7.6%	799	6.8%	1,954	7.3%	1,530	6.6%
Earnings per share-diluted	$0.41	N/A	$0.31	N/A	$0.78	N/A	$0.59	N/A

*   *   *

[O]ur gross margin as a percentage of revenue increased to 18.6% for both the second quarter and first six months of fiscal 2006, compared to 18.2% and 18.1% for the same period in fiscal 2005, respectively. . . . As part of our focus on improving margins, we remain committed to reducing costs . . . . Cost savings initiatives include providing certain customer technical support . . . .

151. Dell's 2ndQ F06 10-Q also contained the Sarbanes-Oxley certifications signed by Schneider and Rollins, detailed at ¶¶269-273.

152. The positive statements made by defendants regarding Dell during 6/05-9/1/05 artificially inflated Dell's stock, which traded as high as $41.99 on 7/20/05. As Dell's stock traded at these artificially inflated levels, Dell's top executives' stock options remained "***in the money***," Dell insiders unloaded more of their stock to profit from their "pump-and-dump" scheme. Between 2/15/05 and 9/7/05, they sold off 3.5 million shares of their Dell stock for $139 million in illegal insider trading proceeds.

153. During 9/05, a further series of negative company-specific revelations concerning Dell occurred in a series of articles and analyst reports that contained and disseminated information that continued to undercut and contradict defendants' prior positive representations:

(a) On 9/3/05, the *New York Times* published a negative article about Dell:

Is Dell a Buy For Consumers Or Investors?

*   *   *

Dell's ability to maintain margins through strong customer service seems to be slipping. In the University of Michigan's latest customer-satisfaction survey, Dell's lead over the rest of the industry – except Apple, which is adored by its small but fiercely loyal base of owners – ***has evaporated***.

Another survey gave the company even lower marks. The sample size was small, however – one person, me – so pedantic, old-school pollsters may question its validity.

I ordered a Dell PC, but when I called back with questions, the transaction could not be found under my name, phone number or ZIP code. Apparently, the order taker hit the trifecta and got them all wrong.

When I expressed my frustration, the rep hung up. I called back, seething, to cancel the purchase, but there was no need. The order taker had also entered my card details incorrectly, so it was never processed.

Jennifer Davis, a Dell spokeswoman, conceded service problems exist at the company . . . .

(b) On 9/5/05, *Business Week* reported:

DELL FINDS ITSELF IN BLOG HELL

PC industry circles have been buzzing for months about slipping customer support at Dell, a claim bolstered on Aug. 16 by a University of Michigan study that showed a hefty drop in customer satisfaction from a year ago. So the last thing Dell needed was for someone to turn the issue into a cause celebre.

Enter Jeff Jarvis. Over the summer the media critic and popular blogger began writing on his personal blog, BuzzMachine, about his lengthy quest to fix a $1,600 computer, an ordeal that, according to him, included countless e-mails, some unanswered, and phone calls to Dell's service line. Jarvis wrote that he bought a service package that included in-home repairs, but when the PC overheated and malfunctioned, he was told to send it in. He did – and wrote that it still wasn't working upon return. Jarvis launched a series of attacks, including an Aug. 17 open letter to CEO Michael Dell: "The bottom line is that a low-price coupon may have gotten me to buy a Dell, but your product was a lemon, and your customer service was appalling." On Aug. 22, Jarvis finally got a refund. A day later he blogged that Dell's new policy of tracking down unhappy bloggers "is a start."

Jarvis' rants struck a chord with other Dell customers. ***Daily visits to BuzzMachine have doubled, to over 10,000 estimates research firm Intelliseek***. . . .

(c) On 9/11/05, *The Sunday Times* published a negative article regarding Dell headlined and stating:

Once-mighty Dell is no longer a world beater

* * *

After years of adulation, Dell faces the kind of criticism usually leveled at its rivals.

* * *

Dell is getting walloped. Once-friendly analysts have doubts about the company's future growth, and its share price is down.

(d) On 9/12/05, *Barron's* published a negative article about Dell stating:

[N]ot everyone feels good about Dell these days, including, most notably, its stockholders.

Investor angst became especially evident last month when Dell reported its second-quarter results for the fiscal year ending January. . . . [S]ales came in 2% below the company's guidance, at $13.4 billion for the three months. ***However tiny, that shortfall was disappointing enough to investors that they slammed the shares down nearly 10% overnight, to $36.64, cutting nearly $10 billion off Dell's market value.***

. . . "***Confidence in the company's ability to perform has seriously shaken the market sentiments***," says Niral Dalal, an analyst with research house First Global.

(e) On 9/12/05, *B to B* published a negative article about Dell's poor customer satisfaction:

How one man's Weblog became Dell's nightmare

What's worse than an unsatisfied customer? How about an unsatisfied customer who is one of the most popular bloggers on the Web?

That's exactly what happened to Dell Computer this summer. What began as a personal account by former mainstream journalist Jeff Jarvis of his problems with Dell on his BuzzMachine blog ***has turned into a public perception nightmare for the Austin, Texas-based computer company***.

Jarvis, a media veteran . . . posted his initial ticked-off commentary about Dell in June. He had bought a Dell laptop that malfunctioned, requiring him to send it back even though he had purchased an expensive in-home service agreement. That first rant got 108 reader comments, with many trading personal stories of unsatisfactory service.

As June went on, Jarvis continued to detail his Dell experiences. He got the computer back, but it still overheated. Then the hard drive broke, and still no

one answered his e-mails. ***He logged all the activity, giving his write-ups such titles as "Dell Sucks. Dell Lies" and "Dell Hell, Continued.***" . . .

. . . The blogging continued to rage, on both Jarvis' site and others, with Jarvis writing an open letter Aug. 17 to Michael Dell and CMO Michael George lamenting their lack of response as well as offering suggestions on how to interact with bloggers. Mainstream media picked up on the story, including BusinessWeek, Fast Company, ZDNet, PC World and the Houston Chronicle.

(f) On 9/29/05, *Moors & Cabot*, a boutique research firm, released a negative report on Dell, focused on Dell's declining customer support and service and customer satisfaction:

[W]e think deteriorating service and support ratings could be a drag for two or more years. . . . [W]e believe disappointing sales and support experiences over the last few years . . . have been a negative for Dell. . . .

. . . ***[T]here have been an increasing number of complaints regarding Dell's service and support for two to three years***. . . .

- **University of Michigan American Customer Satisfaction Index (ACSI)** – In Aug-05, Dell's ACSI rating of 74 fell 6.3% Y/Y and was the company's worst showing since 1998. . . . ***Customer complaints are up significantly with long wait-times, and difficulties with Dell's call-center abound. Consumers are also questioning the reliability of their PCs***."

- **Consumer Reports** – ***Dell's Mar-05 desktop tech support score was 62 out of a possible 100, down from 74 in Dec-01 and 65 in Sep-02***. . . .

- **Technology Business Research** – In TBR's 4Q04 report on support satisfaction among corporate buyers, ***Dell's satisfaction rating slipped to 81.0, down from 83.4 in 3Q03. . . . [I]ts score was the lowest since TBR began tracking Dell's satisfaction levels in 1Q01 and was well below Dell's average rating of 82.9 in TBR surveys***.

(g) On 10/1/05, *Direct* published an article about Dell's poor customer service/satisfaction:

Dell Takes One Hell of a Blogging

Type the phrase "Dell Hell" on Google and the world's most popular search engine returns more than 2.4 million results. Type "Dell sucks" and almost 1.3 million results come back.

Dude, Dell has a problem.

The computer marketing giant has taken a serious battering, in large part because of a summer-long rant on a journalist's personal blog. Jeff Jarvis began writing on BuzzMachine in June about his fruitless efforts to get Dell to fix his malfunctioning computer, a quest he claims included an infuriating string of unanswered or improperly handled e-mails and phone calls.

* * *

In an open letter to Dell, Jarvis wrote: "Your product was a lemon, and your customer service was appalling. . . . Today, when you lose a customer, you don't lose just that customer, you risk losing that customer's friends. And thanks to the Internet and blogs and consumer rate-and-review services, your customers have lots and lots of friends all around the world."

The following day the letter was the third most linked-to post in the blogosphere . . . .

* * *

"***Dell has become worse than a door-to-door salesman," Jarvis wrote. "No pride. No shame. No value. No brand. As I said when all this started: Dell sucks.***"

This story is old news in the blogosphere. For Dell, however, its ramifications probably haven't even begun to emerge.

It's hard to imagine that any consumer doing the slightest amount of online research for their next computer purchase won't stumble across the negative comments about Dell.

And the Internet is littered with posts indicating that Jarvis is far from alone.

* * *

The firm is "past the point of no return," wrote Steve Rubel, vice presidence of client services for public relations firm CooperKatz & Co. of New York, on his blog Micro Persuasion.

(h) On or about 10/3/05, the 10/10/05 edition of *BusinessWeek* published another negative article about Dell's customer service/satisfaction:

Hanging Up On Dell?; Gripes about tech support are on the rise, and the PC king is scrambling to upgrade

It didn't seem as if he was asking for much. When the CD drive on Peter Ulyatt's Dell desktop computer failed this summer, he called the support crew at Dell, where he'd bought the $1,600 machine nine months prior. Armed with an extended warranty that cost him an extra $300, the Pasadena (Calif.) retiree got on

the phone and waited. After sitting on hold for 45 minutes, a technician whom Ulyatt could barely understand came on line and diagnosed a "software problem." Ulyatt's call, transferred to the software technician, was dropped. Calling back, Ulyatt waited on hold another 45 minutes, asked for the software desk, and waited a half-hour more before hanging up. "At the moment, I'm not high on Dell's service," says Ulyatt, who plans to buy two new PCs in a year or so. "***When I buy again, I will look at others beyond Dell.***"

Ulyatt's ordeal is not an isolated case. . . . [R]ecent surveys suggest the ranks of frustrated Dell Inc. owners are growing. Complaints to the Better Business Bureau rose 23% in 2004 from the year before, and they're up another 5% this year. And Dell's customer-satisfaction rating fell 6.3%, to a score of 74, in a survey by the University of Michigan. Dell's score puts it right at the PC industry's average for the study, in which Apple Computer Inc. led the way with an 81. Still, it's a big decline, especially for a company that has often topped the list. "We've never seen a drop like this," says professor Claes Fornell, who ran the survey.

Plenty of people are going public with complaints. Media critic Jeff Jarvis has recounted his frustrations on his blog. Web sites such as ihatedell.net have popped up. Helaina Burton recently spent three hours taking to a half-dozen Dell reps – all to solve the simple problem of a faulty keyboard. ***"I certainly won't buy another product from Dell," she says.*** "I will make sure that any other prospective Dell customer I meet knows what kid of treatment they'll get."

Could such sentiment lead to trouble for the world's largest PC company? ***Over the past decade, Dell's dependable support, combined with competitive prices and build-to-order convenience, made it the default choice for millions of consumers. . . . [A] sagging reputation could slow sales . . . . In the most recent quarter, Dell missed its sales target, one reason its stock has dropped 18%, to $34, since the start of the year.***

* * *

Dell is working to reverse the service slide. John Hamlin, senior vice-president of Dell's U.S. consumer business, ***says the company is hiring a few thousand additional reps this year and striving to reduce call transfers.***

154. As a result of these 9/05 and early 10/05 negative revelations about Dell, which further undermined and contradicted Dell's prior positive statements about its product quality and customer support, service and satisfaction, Dell's stock declined from $35.66 on 9/6/05 to $31.65 on 10/6, a loss of $10 billion in market capitalization, as further artificial inflation came out of the stock, damaging prior Class Period purchases. However, while Dell stock declined in price as a result of these revelations, it remained artificially inflated due to Dell's failure to make

full and truthful disclosure and its continuing to make false and misleading statements. For instance, on 10/20/05, the *Technology Report* published an article about a presentation by M. Dell at a huge conference in Canada:

> **Dell boss bullish on sales growth; Founder sees annual revenue ballooning by $30-billion despite market conditions**
>
> ***Michael Dell doesn't seem to have heard of any slowdown in the technology sector.***
>
> * * *
>
> ***Dell . . . says foreign expansion and sales to more business based customers will help the Round Rock, Tex., company hit $80-billion in sales in the next few years.***
>
> * * *
>
> Mr. Dell . . . ***denies that the company's service is slipping and says Dell continually ranks above its competitors. "Part of the issue is just the sheer number of customers that we're dealing with," he says.***

155. The statements made on 8/11/05, 9/1/05 and 10/20/05, as pleaded above, impacted and were reflected in the market trading price of Dell stock. These statements included:

- Dell's disappointing 2ndQ F06 revenues were due to "***misexecut[ion]***" because Dell "***didn't get up sell within the consumer business***" but that was something "***we can fix***," "***we'll get it back in line***" and "***management had identified and addressed the problem which drove the FQ2 revenue shortfall***."

- Dell had seen "***no slowdown***," the Company's service was not "***slipping***" and the "***Company ranks above its competitors***."

- Dell's 2ndQ F06 operating margin was 8.7% – an improvement – and Dell "***remained committed to reducing costs***" as "***cost savings initiatives include providing . . . customer support functions from cost-effective locations***."

- Dell's top officers had reviewed Dell's internal financial and accounting and disclosure controls. Those controls were effective to assure accurate preparation of Dell's SEC filings and that no undisclosed deficiencies in Dell's internal controls or fraud – material or otherwise – existed at Dell.

These statements were false and misleading. The true undisclosed facts, which were known to or recklessly disregarded by each of the Dell Defendants, were:

(a) The Dell Direct business model was not operating successfully or creating the strong, often record, financial results and operating margins Dell was reporting; in fact, due to overly aggressive cost-cutting in Dell's customer support and service and manufacturing operations, Dell's business model was being afflicted with sky-rocketing customer dissatisfaction and complaints, as well as increasing product quality problems (especially with laptop batteries and capacitors). In truth, Dell's financial results were being falsified and temporarily inflated by (i) large cost-cuts which would have to be reversed and remediated; (ii) improper accounting tricks, including under-accruing warranty costs and failing to take timely write-downs for defective products and product replacement; and (iii) its secret receipt of some $200 million per quarter in rebate/kickback payments from Intel in return for exclusively purchasing Intel microprocessors/chips.

(b) Dell was not manufacturing or selling the highest quality products, as Dell's aggressive cost-cutting in its manufacturing operations to boost its reported profits in the short term had badly weakened Dell's quality control procedures and standards for component parts, *i.e.*, batteries and finished goods, such that Dell was encountering an upsurge in customer complaints due to faulty products, including capacitor failures, motherboard failures and widespread laptop (lithium) battery defects.

(c) Dell did not have an unrivaled ability to create products or technologies that met or exceeded customer expectations, nor did it have world-class manufacturing excellence, producing high-quality products. In fact, as a result of the aggressive cost cuts in Dell's manufacturing operations, Dell's quality assurance procedures had become badly impaired, leading to a marked decline in product quality.

(d) Dell's cost-cutting program was resulting in a marked increase in the production of defective products which did not meet Dell's historic quality standards and a marked decline in Dell's historic levels of customer support and service and thus customer satisfaction, which Dell insiders knew would cost hundreds of millions, if not billions, of dollars to remedy, including the hiring of thousands of additional full-time employees to be trained to staff customer call centers and to improve Dell's quality assurance techniques and practices in its manufacturing operations.

(e) In order to cut operating costs, Dell had sharply curtailed its quality control processes by no longer testing component parts (specifically batteries, hard drives, optical drives or motherboards and laptop accessory parts, including power adaptors) received from suppliers. Rather, Dell was relying on post-assembly quick tests of completed units to discover defective component parts. In addition, it had also curtailed the post-assembly "burn-in" testing of units, which steps in combination were resulting in Dell shipping much larger numbers of computers with defects and performance problems, leading to increased quality problems and customer dissatisfaction.

(f) Dell was not providing superior customer service and support as, due to overly aggressive cost-cutting activities in Dell's customer support and service operations to boost its reported profits in the short term, including moving most of Dell's consumer and small business customer support and service call centers to India and the Philippines and replacing full-time, well-trained employees with part-time, ill-trained (but cheaper) employees, Dell's customer support and service operations were badly impaired, resulting in very long wait times and an inability to adequately respond to customer complaints and questions, generating an upsurge in customer anger and dissatisfaction with Dell, its products and its customer support and service which Dell's internal metrics showed would hurt sales.

(g) Because of its shifting of much of its customer support and service operations, especially for its consumer and small business customers, to "call centers" in India and the Philippines and staffing its call centers with part-time, poorly trained employees, Dell was no longer providing a superior customer experience or generating high degrees of (or improving) customer satisfaction. Rather, Dell was encountering a widespread customer revolt with a massive upsurge in complaints regarding declining product quality and declining service and support operations and a sharp decline in one of Dell's key internal metrics – the "likely to repurchase" number.

(h) The Dell Direct model also was not functioning effectively with respect to Dell's direct sales process because Dell had flooded the market with a huge number of confusing and contradictory promotional offers which its now ill-trained and inadequate sales force was unable to effectively process. This was leading to refusals to honor many "coupons" and "promotions," resulting in customer dissatisfaction and refusal to buy Dell products, which was showing up in an important internal Dell metric known as the "likely to repurchase" number, where Dell was seeing soaring negative sentiment which meant customers were displeased with the Dell sales process and thus Dell's sales growth would decline.

(i) While Dell publicly disseminated favorable surveys and reports purporting to show high degrees of Dell customer satisfaction with product quality and service and support, in fact, its own internal surveys, information and customer metrics (which it constantly monitored) showed a huge upsurge in customer dissatisfaction with and anger at Dell, including a measurable increase in negative responses to its most important metric, the so-called "likely to repurchase" number, which Dell knew indicated serious problems with ongoing sales growth.

(j) Dell's increasing product quality was not resulting in a decrease in Dell's warranty costs. In fact, Dell had quietly curtailed the length of its product warranty and sharply

curtailed the breadth of its warranty coverage (it had eliminated the computer operating system from its warranty) and, in addition, had secretly adopted a new "fix-on-fail-only" policy, whereby it would provide in-home repair service or product replacement only when a computer (or component) completely failed, as opposed to merely malfunctioned, to cut costs. However, these severe restrictions in Dell's warranty and service to its customers – which were much different than Dell's historic "customer friendly" approach to warranty, service and product quality issues – were causing an upsurge in customer dissatisfaction with and anger at Dell, which Dell insiders knew would inevitably result in declining sales growth and a massive increase in warranty and product repair costs to try to restore customers' satisfaction to acceptable levels.

(k) Dell's 2ndQ F06 financial statements were artificially inflated and falsified, as detailed in ¶¶233-273, due to a failure to properly accrue required amounts for warranty costs, failure to recognize large product defect/recall costs and failure to properly disclose the existence, nature and extent of the huge rebate payments Dell was receiving each quarter from Intel.

(l) Dell's Sarbanes-Oxley representations were false, as Dell's internal financial and accounting and disclosure controls were deficient and an undisclosed material fraud was ongoing at Dell – Dell's financial statements were being falsified, its disclosures in its SEC filings were false and misleading and an ongoing fraudulent violation of the securities laws was occurring.

(m) Dell's statements regarding its ability to quickly benefit financially from declines in component part prices was false and misleading. The true reason for Dell's reported superior operating margins was, in large part, the hundreds of millions of dollars of secret and

likely illegal rebate/kickback payments Dell was receiving from Intel at the end of each quarter in return for purchasing 100% or virtually 100% of its microprocessor requirements from Intel.

(n) Due to customer demand for PCs with the advanced features and advantages of the new AMD microprocessor chips, Dell had decided it would have to begin to purchase AMD chips for its computers, which would mean the loss of those hundreds of millions of dollars of rebate/kickback payments from Intel, which would hurt Dell's operating profits and margins.

(o) Dell's U.S. consumer/small business operations were not "going gangbusters," or achieving success, but, in fact, were performing very poorly and well below expectations due, in large part, to the product quality and customer service and support deficiencies outlined above.

(p) The Dell Direct business model was not advantaged in all environments across all regions and in all product categories or able to cause Dell to report solid profits and rapid growth regardless of prevailing market conditions due to product quality and customer service and support issues due to the deficiencies and defects detailed above.

(q) Dell's purported improvements in reducing its operating expenses as a percentage of net revenues and the reported increases in its net and gross operating profit margins to record high levels were only being achieved at the cost of the serious product quality and customer support and service problems outlined above and which the Dell Defendants knew would require massive expenditures to fix, harming Dell's profitability going forward.

(r) Due to the material adverse facts and problems set forth above, Dell and the Dell Defendants knew that Dell could not and would not achieve the revenue, operating profit, operating profit margins, net income and EPS growth being forecast by them.

156. After the close of trading on 10/31/05, Dell again surprised investors – revealing that its financial results for the 3rdQ F06, ending 10/31/05, would be lower than earlier forecast due in part to a sharp fall in its U.S. consumer business and ***a huge $450 million write-off – $.14 per share – mostly due to defective parts in its Optiplex desktop personal computers***. Word also spread of large layoffs – some 1,000 employees. Dell's stock plunged lower on these negative revelations.

157. On 11/1/05, *Bloomberg* reported "Dell Shares Slide as Sales Miss Company's Forecasts":

> Shares of Dell Inc. . . . ***posted their biggest decline in more than four years after the company missed its sales forecast for the second straight quarter.***
>
> At least three analysts . . . lowered their ratings on the stock. Dell said yesterday that preliminary results show ***sales were $13.9 billion compared with the $14.1 billion to $14.5 billion it had predicted.***
>
> . . . ***The missed forecast, following a similar shortfall last quarter, indicates . . . Dell won't be able to repeat the sales growth that averaged 18 percent in the past three years.***
>
> * * *
>
> Dell shares, already down 24 percent this year, fell $2.57 to $29.31 at 10:42 a.m. New York time in Nasdaq Stock Market composite trading and sank as low as $29.13, ***an 8.6 percent drop. That marked the biggest slide since Aug. 17, 2001.***
>
> * * *
>
> Dell said it will also have an expense of $450 million, or 14 cents a share, $300 million of which is associated with costs to service desktop PCs that were built with a faulty part supplied by an unnamed company. The part was in some of the Optiplex PCs it sells to businesses, Dell said, without elaborating.

158. On 11/1/05, *The Wall Street Journal* reported:

> **Dell warns of sales, profit slump – PC maker cites weakness in U.S. Consumer market and swollen inventories.**
>
> DELL INC. warned it would miss its fiscal-third-quarter earnings and sales forecasts, ***blaming continued weakness in its U.S. consumer business*** . . . . ***Dell also said it would take a $450 million charge in the quarter.***

Dell's troubles come at a time when the world-wide personal-computer market is showing strong gains.

159. On 11/1/05, the *Los Angeles Times* reported:

Dell Says Sales Miss Forecasts in 3rd Quarter; The PC maker notes that demand in the U.S. and Britain has been disappointing. It also is taking a charge of $450 million

Dell Inc. said Monday that it would report third-quarter sales below forecasts . . . . The shares dropped 6%.

* * *

Sales growth of 11% in the quarter would be the slowest in more than three years and may dash Rollins' plans to reach $60 billion in sales this year.

"***All of a sudden, long-term growth-rate expectations have ratcheted down***," said Chuck Jones of Atlantic Trust Stein Roe in San Francisco.

* * *

Dell shares have tumbled 19% in less than three months on concern that the company won't be able to maintain its historical pace of sales growth, which averaged 18% in the last three years.

160. On 11/1/05, Moors & Cabot issued a negative report on Dell. It stated:

Downgrading on Numerous, Growing Concerns – Has Dell Lost Its Mojo?

. . . [W]ith the 3FQ miss, ***we now question Dell's ability to get back on its previous track. Thus, we are downgrading the stock . . . and again lowering our estimates*** . . . .

- **Our list of concerns has been growing.** ***We have previously expressed concerns about Dell's . . . customer satisfaction. To this list we now add: . . . concerns Dell has not handled recent product failures well (more on this below), and another quarter of decelerating revenue growth.***

  . . . Dell now expects 3FQ revenue growth of 11% Y/Y, compared to prior guidance of 13-16%.

* * *

- **We believe Dell delayed replacing Optiplex GX270 motherboards that may have had failing capacitors, which could be another blow to its reputation for quality and service.** ***Bulging capacitors, although tough to troubleshoot, fail slowly and thus generally provide early warning flags. Our field checks suggest Dell has***

> ***not been replacing motherboards with bulging capacitors that may been exhibiting symptoms of imminent failure, citing replacement part supply constraints for its "fix on fail" policy.***

161. This negative company-specific information contradicted defendants' prior representations. Dell's stock plunged from $32.15 on 10/31/05 to $28.81 on 11/01/05 on 105 million shares – its biggest one-day decline in several years – a loss of almost $10 billion in market capitalization, as more of the artificial inflation came out of the stock, damaging prior Class Period purchasers. However, Dell's stock continued to trade at artificially inflated, albeit lower, prices, as Dell continued to report false and inflated financial results and continued to make false and misleading statements.

162. On 11/1/05, Dell held a conference call for analysts, money managers and institutional investors to discuss Dell's 3rdQ F06 results. During this call the following occurred:

> [**Jim Schneider –** ***CFO*****:**] Thanks, Lynn. ***While we are disappointed we didn't reach our revenue target for the quarter we are very pleased with our ability to deliver industry-leading profitability [and] consistent growth in earnings*** . . . . In the third quarter . . . ***record earnings grew 18% on a non-GAAP basis.***
>
> * * *
>
> Turning to our results for the third quarter we generated . . . . ***GAAP EPS of $0.25 includ[ing] nonrecurring charges totaling $442 million, or $0.14 per share.***

163. On 11/2/05, *BusinessWeek Online* published an article about Dell, indicating Dell's cost cutting to meet earnings forecasts/targets had hurt Dell's customer support and service, its product quality and its customer satisfaction upon which its Dell Direct model and revenue growth depended. The article was headlined and stated:

> **It's Bad to Worse at Dell;**
>
> ***Projected sales and earnings shortfalls are the latest signs that Dell's days of domination over its PC-industry peers may be coming to an end.***

. . . On Oct. 31, Dell (DELL) said it would fall short of both revenue and earnings expectations for its fiscal third quarter. ***Look beyond the surface, and the long-term situation at the world's largest PC maker may be even worse.***

After years of heady growth, Dell may be coming back to earth. . . . ***[I]t has now missed expectations for two consecutive quarters. The shortfalls are a sign it may be struggling to slash costs enough to maintain rich earnings, while also lowering prices enough to gain share and keep top-line growth racing along.***

* * *

Many observers, including customers, partners, and analysts, fret that Dell may have been cutting costs so much in order to hit financial targets in recent quarters that it has compromised other measures of performance, including customer support and, possibly, product quality.

164. On 11/8/05, Moors & Cabot issued another negative report on Dell:

- ***It could take at least several quarters – and potentially several years – for Dell to find its mojo, in our opinion.***

* * *

- ***. . . Dell's main selling points have historically been low prices and superior customer service and support. Yet surveys show customer satisfaction with Dell's service and support has fallen . . . .***

* * *

Is Turnover Increasing . . . and Causing Customer Satisfaction To Decline?

We believe turnover may be increasing among Dell's sales and support staff and may be causing customer satisfaction issues that may be resulting in Dell losing sales to competing brands.

* * *

As noted previously, we think Dell's customer satisfaction ratings are deteriorating and could be a drag for two or more years. We are particularly bothered by a discrepancy between Dell management's comments and the results of a 3CQ05 Technology Business Research (TBR) study of x86 server customer satisfaction, which shows Dell's ratings continuing a downtrend that began earlier this year. Dell stated recently that it has invested in improving its service and support and that its internal surveys show improvement. Yet TBR noted a marked falloff in Dell's server support scores in 3CQ05, including both phone support and on-site service. This is not consistent with Dell's claims its service and support investments are beginning to pay off.

165. *Fortune's* 11/28/05 edition contained an article stating:

> **The witching hour came, fittingly enough, on Halloween: Dell chief executive Kevin Rollins issued an early warning about the company's third-quarter financial performance**. He probably wished he could hide behind a mask. ***Earnings and sales would both be below expectations. The company would have to write off $450 million, the bulk of it because of an embarrassingly basic misstep for a firm that prides itself on operational efficiency: the installation of faulty capacitors in a large number of computers***. . . .
>
> ***It was not the kind of surprise Dell watchers had come to expect***. For years Dell's startling announcements have been on the positive end, posting blowout revenue numbers, climbing market share, and rocketing profits. Beating Wall Street's expectations had become part of the company's persona . . . .
>
> ***Suddenly though, it seems*** that ***Dell's best days might actually be behind it***. . . . Could this be the end of Dell as we know it?
>
> Founder Michael Dell, still the company's chairman, evinces no apparent unease, despite the fact that his stock is down 28% since August: "There is no perfect linear path to success," he told me. "I think the stock market over-reacted." CEO Rollins goes further: "***No, the sky is not falling at Dell***," he says. . . . ***Our model still works very well***." Changes, Rollins admits, are necessary. But, he says, "***we are not talking about wholesale upheaval. We are tweaking, making refinements and enhancements, and resetting***."

166. On 11/28/05, Dell filed its 3rdQ F06 report on Form 10-Q with the SEC, signed by Hooper. The 10-Q Report contained the same financial results earlier reported and stated:

> Operating income and earnings per share declined year-over-year due to charges of $442 million primarily for warranty costs of $307 million for servicing or replacing certain OptiPlex™ systems that include a vendor part that failed to perform to our specifications.
>
> * * *
>
> Results of Operations.
>
> The following table summarizes the results of our operations for the three and none month periods ended October 28, 2005 and October 29, 2004:

	Three Months Ended 10/28/05 Dollars	% of Revenue	10/29/04 Dollars	% of Revenue	Nine Months Ended 10/28/05 Dollars	% of Revenue	10/29/04 Dollars	% of Revenue
	(in millions, except per share amounts and percentages)							
Revenue	$13,911	100.0%	$12,502	100.0%	$40,725	100.0%	$35,748	100.0%
Gross margin	$2,251	16.2%	$2,313	18.5%	$7,241	17.8%	$6,520	18.2%
Operating expenses	$1,497	10.8%	$1,218	9.7%	$4,140	10.2%	$3,453	9.7%
Operating income	$754	5.4%	$1,095	8.8%	$3,101	7.6%	$3,067	8.6%
Net income	$606	4.4%	$846	6.8%	$2,560	6.3%	$2,376	6.6%
Earnings per share - diluted	$0.25	N/A	$0.33	N/A	$1.03	N/A	$0.92	N/A

* * *

Our gross margin declined for the third quarter of fiscal 2006 . . . . Our year-over-year decline in the third quarter is due to a product charge of $338 million for estimated warranty costs of servicing or replacing certain OptiPlex™ systems that include a vendor part that failed to perform to our specifications, as well as additional charges for product rationalizations and workforce realignment. . . . ***As part of our focus on improving margins, we remain committed to reducing . . . warranty costs . . . . Cost savings initiatives include providing certain customer technical support . . . from cost-effective locations . . . .***

167. Dell's 3rdQ F06 report on Form 10-Q also contained the Sarbanes-Oxley certifications signed by Schneider and Rollins, detailed at ¶¶269-273.

168. On 12/16/05, it was reported that Dell was undertaking a laptop battery recall:

Dell recalls laptop batteries on overheating concerns

. . . Dell Inc. recalled some notebook-computer batteries because of the possibility of overhearing and potential fire risk, the U.S. Consumer Product Safety Commission said Friday.

The consumer watchdog said the recall affects about 22,000 batteries in the United States sold individually and with certain Dell laptop models between Oct. 5, 2004, and Oct. 13, 2005.

* * *

The recall was triggered by three reports of batteries overheating that caused damage to a tabletop, a desktop, and resulted in minor damage to personal items, the commission said.

169. The 12/16/05 battery recall, coming on the heels of the negative disclosures and publicity concerning Dell's products, confirmed the existence of those quality problems and indicated that Dell's product quality problems were likely more widespread than earlier revealed. Dell's stock fell from $33.06 on Friday, 12/16/05, to $30.82 on Wednesday, 12/21/05 – three trading days later. This loss of over $5 billion in market capitalization caused some of the artificial inflation to come out of Dell's stock price, damaging prior Class Period purchasers.

170. On 2/16/06, Dell reported 4thQ F06 and F06 results that again disappointed investors with lower-than-forecast sales and profit growth and much lower-than-expected gross margins. During a 2/16/06 conference call, Rollins made admissions that the cost to Dell of trying to restore Dell's damaged customer support and service operations and to try to restore customer satisfaction would be substantial. He said:

> Turning to the customer, we ceded some ground on a core attribute of our Dell direct model, and that is our unparalleled customer satisfaction experience. . . . [W]e deem this unacceptable . . . .
>
> ***To address capacity issues, we've opened or announced 10 global contact centers, including Oklahoma City, Edmonton, Manila, Halle and Gurgaon, India. To improve hold times, we increased our Americas telephone support staff by approximately 20%, and our E-support staff by approximately 60%.***
>
> * * *
>
> The Company expects first quarter fiscal year 2007 . . . earnings per share of 39 cents to 41 cents . . . .

171. On 2/16/06, Bear Stearns reported:

> [M]argins deteriorated as Dell traded revs for profits in consumer . . . .
>
> . . . DELL's ***revenue outlook was disappointing, implying deceleration to 6%-9% YoY growth*** . . . .
>
> * * *
>
> *** Reflecting Dell's weaker 1Q07 outlook, ***we're lowering ests for FY07 . . . and for FY08*** . . . .

* * *

- ***Gross margin declines sharply.* Gross Margin of 17.84% was well below our estimate of 18.48% by 65 basis points, down 75 basis points sequentially and 70 basis points from the prior year period . . . .**

172. On 2/17/06, *The Mercury News* reported:

The heady days of double-digit growth at Dell Inc. may be numbered.

* * *

Sales . . . rose a . . . modest 13 percent . . . .

On top of that, Dell offered a first-quarter outlook that called for a revenue gain of 6 percent to 9 percent. The forecast drew lots of attention Thursday because it was less than analysts were expecting and because Dell routinely promised increases in the mid-teens just a few quarters ago.

173. On 2/17/06, *Bloomberg* reported:

Shares of Dell Inc. fell the most in more than three months, on concern that the company may have sliced prices to drive sales last quarter after missing its revenue forecast twice last year. . . .

. . . Dell was a "***little bit more aggressive in pricing***" on products including notebook PCs to win orders, Chief Financial Officer Jim Schneider said yesterday.

* * *

. . . ***Profit and sales forecasts for this quarter fell short of projections. Dell said sales growth would slow to 6 percent to 9 percent from 16 percent a year ago.***

The company's shares sank $1.58, or 4.9 percent, to $30.38 at 4 p.m. New York time in Nasdaq Stock Market composite trading.

174. On 2/17/06, SG Cowen & Co. issued a report on Dell:

Puzzling Q4-Q1 Sequence

. . . ***[G]uidance for Q1 is puzzlingly weak, looked at either Y/Y or vs actual . . . . We are reducing EPS for F07 by a nickel . . . there seems to be a bit of trouble in paradise . . . .***

. . . ***While management defends integrity of model advantages over competition . . . hard not to question whether edge has narrowed.***

175. On 2/21/06, suddenly and without warning, Dell postponed its annual meeting with analysts/investors scheduled for 4/06 in Austin, Texas, until 9/06. On 2/22/06, *MarketWatch* reported:

Dell shares fall in pre-market trades; analyst day postponed

. . . Dell Inc. shares fell about 1% in pre-market trading Wednesday after the No. 1 maker of personal computers postponed its annual analyst meeting, usually held in April, until September. The stock traded down 1.1% to $29.48 on Instinet trading volume that put it among the 10 most active stocks. . . . Dell shares fell 5% last Friday after the firm reported fiscal fourth-quarter PC sales were flat from a year earlier and issued a financial forecast that lagged the expectations of Wall Street analysts.

176. On 2/22/06, JP Morgan issued a report on Dell:

Dell Cancels Analyst Day, Raises Some Near-Term Concerns

- Last night Dell cancelled its analyst day scheduled for April, and rescheduled for September 2006. ***The abrupt cancellation of the meeting, just days after the company highlighted the event on its earnings call, clearly raises some concerns.***

177. On 2/22/06, Bernstein issued a report on Dell:

Following Dell's disappointing earnings last week, this research piece discusses what we believe are the four key issues coming out of Dell's results.

- **Contrary to our and others' expectations, Dell did not gain overall PC share in Q4 – which was a big disappointment and is likely to fuel continued debate about Dell's sustainable growth rate.** The biggest issue coming out of Dell's Q4 results is that Dell didn't gain PC share in the quarter, despite the fact that its gross margins declined meaningfully and the company had an extra week in the quarter. ***We note that IDC and Gartner calendar Q4 05 data – which showed Dell was gaining share – was misrepresentative, as Dell's submitted data to the groups included an extra week*** . . . .

- **Dell's weakness in consumer is pronounced, which we believe is – in part – attributable to weaker product offerings, particularly consumer notebooks.** We note that Dell's US consumer growth rate has declined from 20%+ to 1% since the beginning of FY2004, and that its operating profit has fallen from 6%+ to 3.8%. ***Our analysis also suggests that US consumer gross margins fell by a startling 200 bps sequentially.***

* * *

- **The strong erosion in Q4 margins . . . is confounding . . . .**

178. Due to the negative, company-specific revelations regarding Dell between 2/16/06 and 2/22/06, Dell's stock fell from $32.24 on 2/15/06 to $28.88 on 2/24/06. This decline caused an $8 billion loss in market capitalization as more of the artificial inflation came out of Dell's stock damaging prior Class Period purchasers. However, while Dell stock declined in price as a result of these revelations, it remained artificially inflated due to Dell's failure to make full and truthful disclosure and its dissemination of false and misleading statements.

179. The statements of 10/31/05, 11/1/05, 11/28/05 and 2/16/06 impacted and were reflected in the market trading price of Dell stock. These statements included:

- Dell's 3rdQ F06 and 4thQ F06 financial results.
- Dell's top officers had reviewed Dell's internal financial and accounting and disclosure controls. Those controls were effective to assure accurate preparation of Dell's SEC filings and that no undisclosed deficiencies in Dell's internal controls or fraud – material or otherwise – existed at Dell.
- ***Dell was "very pleased with [its] ability to deliver industry-leading profitability [and] consistent growth in earnings***" and that in the third quarter the Company's "***record earnings grew 18% on a non-GAAP basis.***"
- Dell had taken steps sufficient to "address capacity issues" and to "improve hold times."
- Dell expected "first quarter fiscal year 2007 . . . earnings per share of 39 cents to 41 cents."

These statements were false. True undisclosed facts, which were known to or recklessly disregarded by each of the Dell Defendants, were:

(a) The Dell Direct business model was not operating successfully or creating the strong, often record, financial results and operating margins Dell was reporting; in fact, due to overly aggressive cost-cutting in Dell's customer support and service and manufacturing operations, Dell's business model was being afflicted with sky-rocketing customer dissatisfaction and complaints, as well as increasing product quality problems (especially with

laptop batteries and capacitors). In truth, Dell's financial results were being falsified and temporarily inflated by (i) improper accounting tricks, including under-accruing warranty costs and failing to take timely write-downs for defective products and product replacement; and (ii) its secret receipt of some $200 million per quarter in rebate/kickback payments from Intel in return for exclusively purchasing Intel microprocessors/chips.

(b) The Dell Direct model also was not functioning effectively with respect to Dell's direct sales process because Dell had flooded the market with a huge number of confusing and contradictory promotional offers which its now ill-trained and inadequate sales force was unable to effectively process. This was leading to refusals to honor many "coupons" and "promotions," resulting in customer dissatisfaction and refusal to buy Dell products, which was showing up in an important internal Dell metric known as the "likely to repurchase" number, where Dell was seeing soaring negative sentiment which meant customers were displeased with the Dell sales process and thus Dell's sales growth would decline.

(c) Dell's increasing product quality was not resulting in a decrease in Dell's warranty costs. In fact, Dell had quietly curtailed the length of its product warranty and sharply curtailed the breadth of its warranty coverage (it had eliminated the computer operating system from its warranty) and, in addition, had secretly adopted a new "fix-on-fail-only" policy, whereby it would provide in-home repair service or product replacement only when a computer (or component) completely failed, as opposed to merely malfunctioned, to cut costs. However, these severe restrictions in Dell's warranty and service to its customers – which was much different than Dell's historic "customer friendly" approach to warranty, service and product quality issues – were causing an upsurge in customer dissatisfaction with and anger at Dell, which Dell insiders knew would inevitably result in declining sales growth and a massive

increase in warranty and product repair costs to try to restore customers' satisfaction to acceptable levels.

(d) The SEC had notified Dell it was investigating Dell's prior financial reporting practices and SEC filings which Dell's top insiders knew would likely uncover numerous irregularities, including under-accruals of warranty obligations, revenue recognition improprieties and concealment of the Intel rebate/kickback payments.

(e) Notwithstanding the large 3rdQ F06 write-down, Dell's 3rdQ F06 and 4thQ F06 financial results and statements remained artificially inflated and falsified, as detailed in ¶¶233-273, due to a failure to properly accrue required amounts for warranty costs, failure to recognize material product defect/recall costs and failure to properly disclose the existence, nature and extent of the huge rebate payments Dell was receiving each quarter from Intel.

(f) Dell's Sarbanes-Oxley representations were false, as Dell's internal financial and accounting and disclosure controls were deficient and an undisclosed material fraud was ongoing at Dell – Dell's financial statements were being falsified, its disclosures in its SEC filings were false and misleading and an ongoing fraudulent violation of the securities laws was occurring.

(g) Due to customer demand for PCs with the advanced features and advantages of the new AMD microprocessor chips, Dell had decided it would have to begin to purchase AMD chips for its computers, which would mean the loss of those hundreds of millions of dollars of rebate/kickback payments from Intel, which would hurt Dell's operating profits and margins.

180. In or about 3/06, Dell issued its F06 Annual Report. It contained a reassuring letter from M. Dell and Rollins, stating:

In fiscal 2006, Dell continued to outpace the industry worldwide and in every region where we compete – ***achieving company records for . . . revenue, operating income and earnings per share***.

Each milestone resulted from the global execution of our direct business model. It continues to give us a one-of-a-kind ability to listen to millions of customers daily, deliver what each defines as value and provide a superior experience.

No other technology company can rival Dell's know-how . . . [in] ***delivering relevant technologies that meet or exceed customer expectations.***

*   *   *

Customer Experience

. . . ***At Dell, an exceptional customer experience begins with product leadership. And it continues long after the sale as we strive to instill satisfaction, trust and loyalty with each customer contact. Sustaining that continuum has been integral to our success.***

*   *   *

We improved Dell's overall customer experience considerably in fiscal 2006. . . .

*   *   *

We continue to reaffirm the tenets of our direct model: . . . ***world-class manufacturing;*** . . . and ***execution excellence***.

181. Dell's F06 Annual Report included the following financial results and financial statements which had been audited and certified by PWC:

OPERATING RESULTS (in millions, except per-share data)		
Fiscal-year ended	Feb. 3, 2006	Jan. 28, 2005
Net revenue	$ 55,908	$ 49,205
GAAP gross margin	$ 9,950	$ 9,015
GAAP operating income	$ 4,347	$ 4,254
GAAP net income	$ 3,572	$ 3,043
GAAP earnings per common share	$ 1.46	$ 1.18

182. On 3/15/06, Dell filed its F06 Annual Report on Form 10-K, which was signed by Schneider, Miles, Carty, Rollins and M. Dell. It contained Dell's F06 financial results and statements as audited and certified by PWC. The 10-K stated:

> **Business Strategy**
>
> Dell's business strategy combines its direct customer model with a highly efficient manufacturing and supply chain management organization . . . . ***This strategy enables Dell to provide customers with*** . . . ***high-quality*** . . . ***technology*** [***and***] ***superior service and support*** . . . .

183. The F06 10-K also included management's discussion and analysis of financial condition and results of operation. It stated:

> **Gross Margin**
>
> The following table presents information regarding our gross margin during each of the past three fiscal years:

	Fiscal Year Ended					
	February 3, 2006		**January 28, 2005**		**January 30, 2004**	
	Dollars	**% of Revenue**	**Dollars**	**% of Revenue**	**Dollars**	**% of Revenue**
	(in millions, except percentages)					
Revenue	$55,908	100.0%	$49,205	100.0%	$41,444	100.0%
Gross Margin	9,950	17.8%	9,015	18.3%	7,552	18.2%

> In fiscal 2006, our gross margin declined as a percentage of revenue . . . . Our year-over-year decline is primarily due to a product charge of $338 million for estimated warranty costs of servicing or replacing certain OptiPlex™ systems that included a vendor part that failed to perform to our specifications . . . . In fiscal 2005, gross margin as a percentage of net revenue improved slightly to 18.3% compared to 18.2% for fiscal 2004. ***This year-over-year improvement was primarily driven by our continued cost savings initiatives.***
>
> As part of our focus on improving margins, we remain committed to reducing . . . warranty costs . . . . ***Cost savings initiatives include providing certain customer technical support*** . . . ***from cost-effective locations*** . . . .

184. Dell's F06 10-K also stated:

> Dell's manufacturing process consists of assembly, software installation, functional testing, and quality control. Testing and quality control processes are also applied to components, parts, and subassemblies obtained from third-party suppliers. Quality control is maintained through the testing of components, subassemblies, and systems at various stages in the manufacturing process. Quality control also includes a burn-in period for completed units after assembly,

on-going production reliability audits, failure tracking for early identification of production and component problems, and information from Dell's customers obtained through services and support programs. . . .

Dell purchases materials, supplies, and product components from a large number of suppliers. . . . Dell currently relies on Intel Corporation as a sole source supplier of processors . . . . These relationships and dependencies have not caused material disruptions in the past, ***and Dell believes that any disruptions that may occur would not disproportionately disadvantage Dell relative to its competitors***.

* * *

Through our direct business model, we design, develop, manufacture, market, sell, and support a broad range of information technology systems and services . . . . Our direct model begins and ends with our customers . . . . ***The unique strengths of our direct model facilitate our consistent delivery of profitability and strong performance across our business segments.***

* * *

Operating Expenses

The following table presents information regarding our operating expenses during each of the past three fiscal years:

	Fiscal Year Ended (in millions, except percentages)					
	2/3/06		**1/28/05**		**1/30/04**	
	Dollars	% of Revenue	Dollars	% of Revenue	Dollars	% of Revenue
Operating Expenses:						
Selling, general, and administrative	$5,140	9.2%	$4,298	8.7%	$3,544	8.6%
Research, development, and engineering	$463	0.8%	$463	1.0%	$464	1.1%
Total operating expenses	$5,603	10.0%	$4,761	9.7%	$4,008	9.7%

* * *

Critical Accounting Policies

We prepare our financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP"). . . . We believe our most critical accounting policies relate to revenue recognition [and] warranty accruals . . . .

* * *

> *Warranty* – We record warranty liabilities at the time of sale for the estimated costs that may be incurred under its limited warranty. . . . Warranty claims are relatively predictable based on historical experience of failure rates. If actual results differ from our estimates, we revised our estimated warranty liability to reflect such changes. Each quarter, we reevaluate our estimates to assess the adequacy of the recorded warranty liabilities and adjust the amounts as necessary.

185. Dell's F06 Form 10-K also stated:

> **ITEM 1B –UNRESOLVED STAFF COMMENTS**
>
> **None.**

186. The statements in Dell's F06 10-K impacted and were reflected in the market trading price of Dell stock. These statements included:

- Dell had achieved "***record***" F06 financial results, including operating income and earnings, which was "***primarily driven by our continued cost savings initiatives.***" These results reflected properly determined "warranty liabilities" which Dell had made "***each quarter***" "***adjusting as necessary***" – Dell faced no unresolved SEC comments.

- Dell's record F06 results came from "***global execution of our direct business model***" and "***no other . . . company***" "***can rival Dell's know-how in delivering***" products "***that meet or exceed customer expectations,***" and Dell had "***improved Dell's overall customer experience considerably in fiscal 2006.***"

- Dell had "***world class manufacturing***" as part of its "***execution excellence,***" generally "***high quality technology***" and "***superior service and support.***"

- Any "***disruption***" of Dell's Intel sole source relationship "***would not disproportionately disadvantage Dell relative to its competitors.***"

- Dell's top officers had reviewed Dell's internal financial and accounting and disclosure controls. Those controls were effective to assure accurate preparation of Dell's SEC filings and that no undisclosed deficiencies in Dell's internal controls or fraud – material or otherwise – existed at Dell.

These statements were false and misleading. The true undisclosed facts, which were known to or recklessly disregarded by each of the Dell Defendants, were:

(a) The Dell Direct business model was not operating successfully or creating the strong, often record, financial results and operating margins Dell was reporting; in fact, due to overly aggressive cost-cutting in Dell's customer support and service and manufacturing

operations, Dell's business model was being afflicted with sky-rocketing customer dissatisfaction and complaints, as well as increasing product quality problems (especially with laptop batteries and capacitors). In truth, Dell's financial results were being falsified and temporarily inflated by (i) improper accounting tricks, including under-accruing warranty costs and failing to take timely write-downs for defective products and product replacement; and (ii) its secret receipt of some $200 million per quarter in rebate/kickback payments from Intel in return for exclusively purchasing Intel microprocessors/chips.

(b) Dell was not manufacturing or selling high quality products, as Dell's aggressive cost-cutting in its manufacturing operations to boost its reported profits in the short term had badly weakened Dell's quality control procedures and standards for component parts, *i.e.*, batteries and finished goods, such that Dell was encountering an upsurge in customer complaints due to faulty products, including capacitor failures, motherboard failures and widespread laptop (lithium) battery defects.

(c) Dell did not have an unrivaled ability to create products or technologies that met or exceeded customer expectations, nor did it have world-class manufacturing excellence, producing high-quality products. In fact, as a result of the aggressive cost cuts in Dell's manufacturing operations, Dell's quality assurance procedures had become badly impaired, leading to a marked decline in product quality.

(d) Dell's cost-cutting program was resulting in a marked increase in the production of defective products which did not meet Dell's historic quality standards and a marked decline in Dell's historic levels of customer support and service and thus customer satisfaction, which Dell insiders knew would cost hundreds of millions, if not billions, of dollars to remedy, including the hiring of thousands of additional full-time employees to be trained to

staff customer call centers and to improve Dell's quality assurance techniques and practices in its manufacturing operations.

(e) Dell was not providing superior customer service and support as, due to overly aggressive cost-cutting activities in Dell's customer support and service operations to boost its reported profits in the short term, including moving most of Dell's consumer and small business customer support and service call centers to India and the Philippines and replacing full-time, well-trained employees with part-time, ill-trained (but cheaper) employees, Dell's customer support and service operations were badly impaired, resulting in very long wait times and an inability to adequately respond to customer complaints and questions, generating an upsurge in customer anger and dissatisfaction with Dell, its products and its customer support and service which Dell's internal metrics showed would hurt sales.

(f) In order to cut operating costs, Dell had sharply curtailed its quality control processes by no longer testing component parts (specifically batteries, hard drives, optical drives or motherboards and laptop accessory parts, including power adaptors) received from suppliers. Rather, Dell was relying on post-assembly quick tests of completed units to discover defective component parts. In addition, it had also curtailed the post-assembly "burn-in" testing of units, which steps in combination were resulting in Dell shipping much larger numbers of computers with defects and performance problems, leading to increased quality problems and customer dissatisfaction.

(g) Because of its shifting of much of its customer support and service operations, especially for its consumer and small business customers, to "call centers" in India and the Philippines and staffing its call centers with part-time, poorly trained employees, Dell was no longer providing a superior customer experience or generating high degrees of (or improving) customer satisfaction. Rather, Dell was encountering a widespread customer revolt

with a massive upsurge in complaints regarding declining product quality and declining service and support operations and a sharp decline in one of Dell's key internal metrics – the "likely to repurchase" number.

(h) The Dell Direct model also was not functioning effectively with respect to Dell's direct sales process because Dell had flooded the market with a huge number of confusing and contradictory promotional offers which its now ill-trained and inadequate sales force was unable to effectively process. This was leading to refusals to honor many "coupons" and "promotions," resulting in customer dissatisfaction and refusal to buy Dell products, which was showing up in an important internal Dell metric known as the "likely to repurchase" number, where Dell was seeing soaring negative sentiment which meant customers were displeased with the Dell sales process and thus Dell's sales growth would decline.

(i) While Dell publicly disseminated favorable surveys and reports purporting to show high degrees of Dell customer satisfaction with product quality and service and support, in fact, its own internal surveys, information and customer metrics (which it constantly monitored) showed a huge upsurge in customer dissatisfaction with and anger at Dell, including a measurable increase in negative responses to its most important metric, the so-called "likely to repurchase" number, which Dell knew indicated serious problems with ongoing sales growth.

(j) Dell's increasing product quality was not resulting in a decrease in Dell's warranty costs. In fact, Dell had quietly curtailed the length of its product warranty and sharply curtailed the breadth of its warranty coverage (it had eliminated the computer operating system from its warranty) and, in addition, had secretly adopted a new "fix-on-fail-only" policy, whereby it would provide in-home repair service or product replacement only when a computer (or component) completely failed, as opposed to merely malfunctioned, to cut costs. However, these severe restrictions in Dell's warranty and service to its customers – which was much

different than Dell's historic "customer friendly" approach to warranty, service and product quality issues – were causing an upsurge in customer dissatisfaction with and anger at Dell, which Dell insiders knew would inevitably result in declining sales growth and a massive increase in warranty and product repair costs to try to restore customers' satisfaction to acceptable levels.

(k) Dell's F06 financial statements were artificially inflated and falsified, as detailed in ¶¶233-273, due to a failure to properly accrue required amounts for warranty costs, failure to recognize large product defect/recall costs and failure to properly disclose the existence, nature and extent of the huge rebate payments Dell was receiving each quarter from Intel.

(l) Dell's Sarbanes-Oxley representations were false, as Dell's internal financial and accounting and disclosure controls were deficient and an undisclosed material fraud was ongoing at Dell – Dell's financial statements were being falsified, its disclosures in its SEC filings were false and misleading and an ongoing fraudulent violation of the securities laws was occurring.

(m) Dell's statements regarding its ability to quickly benefit financially from declines in component part prices was false and misleading. The true reason for Dell's reported superior operating margins was, in large part, the hundreds of millions of dollars of secret and likely illegal rebate/kickback payments Dell was receiving from Intel at the end of each quarter in return for purchasing 100% or virtually 100% of its microprocessor requirements from Intel.

(n) Due to customer demand for PCs with the advanced features and advantages of the new AMD microprocessor chips, Dell had decided it would have to begin to purchase AMD chips for its computers, which would mean the loss of those hundreds of millions

of dollars of rebate/kickback payments from Intel, which would hurt Dell's operating profits and margins.

(o) Dell's purported improvements in reducing its operating expenses as a percentage of net revenues and the reported increases in its net and gross operating profit margins to record high levels were only being achieved at the cost of the serious product quality and customer support and service problems outlined above and which the Dell Defendants knew would require massive expenditures to fix, harming Dell's profitability going forward.

187. The 4/15/06 edition of *The Economist* – published on or about 4/10/06 – contained an article about the AMD suit against Intel, regarding Intel's secret and possibly illegal rebate/payments to customers like Dell with Intel exclusive supply agreements, for the first time calling the payments a "kickback." It stated:

> **Intel inside; Antitrust**
>
> The world's biggest chipmaker is about to have its day in court
>
> * * *
>
> At issue . . . is Intel's use of rebates and marketing funds, which AMD claims is anti-competitive. Intel is accused of discounting its chips in such a way as to make it extremely costly for computer-makers to buy from it anything short of their total requirement. . . . ***Moreover, Intel gives rebates to computer-makers each quarter. In such a low-margin business, these can make a big difference***. . . .
>
> . . . ***The question, however, is whether the programme is simply a kickback mechanism to reward PC-makers for their loyalty to Intel*** . . . .

188. Dell's stock fell from $29.95 on 4/10/06 to $26 on 4/25/06 – 11 trading days – a $10 billion loss of market capitalization as more of the artificial inflation came out of Dell's stock, damaging prior Class Period purchasers.

189. The 7/3/06 edition of *BusinessWeek* contained the following information, revealing that Dell had ***had to hire over 8,000 new employees to try to fix its customer***

service/support problems – a huge number – much larger than earlier disclosed – as Dell reported having 65,200 employees at 2/3/06:

What Dell is Doing to Win Back Customers

Re "Satisfaction not guaranteed" and "Dell: Facing up to past mistakes" (News: Analysis & Commentary, June 19): ***We have acknowledged that our service and support for consumer customers did not keep pace in the rapid growth of that market two years ago. Regrettably, we let some of our customers down. Dell's efforts to restore customer satisfaction include hiring 8,000 new service agents over a three-year period and providing additional training to current agents in our network of 30 global call centers*** . . . .

190. On 6/21/06 and 7/4/06, *The Inquirer*, an Internet publication, reported two serious Dell laptop burning incidents due to battery defects. On 7/6/06, Moors & Cabot issued a report on Dell, more widely publicizing negative Dell battery incidents:

A Second – and Third – Hunk, a Hunk of Burning Laptop

. . . The Inquirer, which broke the story of a Dell laptop bursting into flames during a conference in Japan, has published a report on two additional burning Dell laptops. Should this story also hit the mainstream press, ***we believe there is headline risk and potentially negative demand ramifications for Dell. Reiterate Sell rating***.

- **On July 4th *The Inquirer* published "My Dell Blew Up Too",** a letter from Rich S. in Pittsburgh. According to Mr. S, a Dell notebook that he bought late last year caught fire under normal use at home in Feb-06. He returned the unit to Dell, who told him the fault was the system board. Mr. S reports that after about three months, a replacement laptop from Dell started having similar problems. Mr. S removed power when it started smoking and discovered "burnt material . . . and smoke residue" covering the memory. According to Mr. S, Dell's repair center examined the second laptop and told him a fire had occurred on the system board.

- **Potential headline risk and potential negative demand ramifications reinforce confidence in our Sell rating.** The story of the burning laptop in Japan eventually made its way in Reuters and USA Today. Should this more recent story do the same, we think it could negatively impact demand for Dell PCs.

- **For several reasons, we believe this second story of burning Dell laptops could have more impact than its June 21st predecessor.**

191. On 7/10/06, *The New York Times* reported these increasing adverse battery incidents in Dell's computers:

Dell's Exploding Computer and Other Image Problems

A Dell notebook computer that burst into flames last month in Osaka, Japan, has damaged more than just the conference table where it was smoldering. ***The incident, publicized in photos on the Internet, has also hurt Dell's recent attempts to improve its image.***

The company said the incident got more publicity than such incidents usually do when they happen to other manufacturers. ***In part, that is because Dell's reputation for responsive customer service was already under attack after the company, the world's largest PC manufacturer, started to cut costs at its call centers last year. Dell, reacting to the savaging it has received on blogs and Web sites over the cuts, recently responded with a program to spend more than $100 million to improve service.***

Photos of the flaming and smoking notebook were posted on a technology news Web site called the Inquirer on June 21. The story was passed around to other Web sites and blogs like Consumerist.com. It was also the subject of a brief article carried later that day on the Dow Jones Newswires.

Two days later, Cindy Shaw, a securities analyst with Moors & Cabot, notified her clients about the publicity. Last Thursday, citing reports of a second smoking laptop, this one in Pennsylvania, she advised them that "***should this story also hit the mainstream press, we believe there is headline risk and potentially negative demand ramifications for Dell.***"

* * *

Dell said its engineers examined and tested what remained of the flaming notebook computer for several days to find the source of the problem. They concluded that the fire was caused by a faulty lithium ion battery cell, ***but that the problem was unrelated to a recall last year of notebook batteries by the company and several other computer makers***.

* * *

Dell said that it found no pattern of battery failure and that the Pennsylvania incident publicized by the Inquirer Web site was caused by a chip problem and not batteries.

The company ***also directed reporters' attention*** to a statement by Norm England, chief executive of the Portable Rechargeable Battery Association, that said, "***Based on the millions of lithium ion batteries in use today and the exceptionally small number of cases in which a battery malfunction has occurred, we believe these batteries are safe and reliable***."

192. As this company-specific negative information entered and was digested by the market, Dell's stock fell further – from $24.68 on 7/3/06 to $21.67 on 7/13/06, an $8 billion market capitalization loss, as more of the artificial inflation came out of Dell's stock, damaging prior Class Period purchasers. However, due to Dell's continued false statements, Dell's stock continued to trade at artificially inflated, albeit lower, prices.

193. On 7/11/06, major changes in Dell's consumer sales practices and consumer warranty program were announced:

(a) On 7/14/06, the *Financial Times* reported:

> **Dell Cuts Rebates to Boost Flagging Growth**
>
> Dell, the world's biggest personal computer maker, yesterday moved to simplify its pricing structure by cutting rebates and other promotional offers to personal and small business customers.
>
> The move marks the latest in a series of attempts to adjust the price structure at the computer maker after pricing mistakes contributed to missed forecasts in three of the past four quarters.

(b) On 7/14/06, *The Dallas Morning News* reported:

> ***Dell Inc. will cut back on mail-in rebates and other promotional discounts because the deals confuse customers, the company said Thursday.***
>
> * * *
>
> ***Dell has . . . reversed changes on its warranties in response to customers' wishes, it said. The company increased its basic warranty on Inspiron and Dimension models back to one year from 90 days. And it reinstated warranty coverage for the computer's operating system.***

(c) On 7/14/06, *Investor's Business Daily* reported:

> **Dell Looks To Simplify Shopping By Cutting Back On Rebate Plans**
>
> Personal computer giant Dell plans to pare its use of mail-in rebates as part of a move to simplify pricing and ***boost customer satisfaction***.
>
> * * *
>
> ***Many customers don't like the rebate process and are confused by all the various promotions.***

* * *

Dell also changed the terms of its warranties . . . in response to customer complaints.

It had cut its warranty coverage from one year to 90 days. Dell restored the original terms and will once again respond to operating system issues under its hardware warranties – a service it had offered in the past.

194. As this information indicating serious problems in Dell's consumer sales and product warranty practices was revealed to and digested by the securities markets, Dell's stock fell from $22.68 on 7/13/06 to $20.97 on 7/18/06, three trading days later – a loss of $6 billion in market capitalization, as more of the artificial inflation came out of the stock price, damaging prior Class Period purchasers.

195. On 7/20/06, Dell again shocked investors with further negative revelations inconsistent with and undermining its prior Class Period representations, including warning of another ***huge financial performance shortfall and declining EPS***! On 7/21/06, *The Dallas Morning News* reported:

Dell shares tumble after warning on earnings

Investors hammered Dell Inc. shares Friday after the computer maker fell short again on its earnings forecast.

* * *

Dell projected fiscal second-quarter earnings per share of 21 to 23 cents on sales of $14 billion. In May, the company had predicted its second-quarter figures would be similar to the first quarter, when it earned 33 cents per share on sales of $14.2 billion.

Dell's stock took a dive from the moment the opening bell sounded on Wall Street.

196. On 7/21/06, JP Morgan issued a report on Dell:

Major Structural and Strategic Changes in Order

* * *

- ***This shortfall is far more significant than our previous thesis could have envisioned.*** We had assumed that Dell's problems were confined to its U.S. Consumer business, but this quarter's shortfall in commercial suggests we were wrong.

* * *

- At this point, we believe that major structural and strategic actions are necessary to begin a bottoming process for the stock. These changes should include, but not be limited to the following: substantial changes in business leadership structure; ***significant refinements to the direct model in the consumer space*** . . . .

197. On 7/21/06, Moors & Cabot issued a report on Dell, indicating that Dell's customer service and support problems had not been remedied and were getting worse and its customer satisfaction was not improving, but worsening:

Better Business Bureau (BBB) Complaints Shed Light on Dell's Challenges

. . . Based on BBB data, we believe customer satisfaction may be more than an order of magnitude lower for Dell consumers than for H-P consumers after adjusting for market share. We are reducing estimates and our price target to reflect increasing concern about Dell's customer experience challenges and ability to succeed given current market trends.

- BBB data suggests to us that Dell's customer experience challenges are extensive. Indeed, the BBB's website states "The BBB has recently met with Dell Inc. to develop a better understanding of their policies and to discuss the complaint activity." The BBB does not make similar comments about H-P or Gateway. Based on BBB data, we estimate that for every PC or printer sold to a U.S. consumer a Dell customer may be about 2.5 times as likely to complain to the BBB as a Gateway customer and possibly sixteen times as likely as an H-P customer.

* * *

- Reducing EPS estimates . . . . We are reducing EPS estimates to reflect (1) greater concerns about Dell's challenges in the consumer segment, which accounted for 9% of FY06 operating profit . . . .

Consumer May Be About 16x as Likely to Complain to the BBB about Dell than about H-P

* * *

Because the BBB serves primarily U.S. consumers and very small businesses (which we believe behave like consumers when it comes to computer equipment),